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Senior Consultant

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What Is The New Economy?

Robert Morgenthau

The new economy is about the radical effects of information on the economy as a whole. What then, is the impact of the information-driven new economy on companies? Where might the consulting business head as a result of the continuing shift into the new economy, and how should we confront these issues?

The concept of a new economy remains somewhat controversial because it has too often been used as an excuse for throwing out all of the old rules, many of which clearly haven't worked over the past decade. The reason those "old rules" haven't worked is that, for the past ten years, the economy has been different in several key respects: There has been a period of sustained growth in GDP, unemployment is falling, and inflation has been steady. These simultaneous events contradict the biggest old rule of all – that increased productivity usually creates high inflation. The impact of this unusual combination has led to enormous markets and a never-before-seen level of economic prosperity. And information technology (comprising technology, telecommunications and the internet) has played a crucial role in creating these factors, changing the landscape of business worldwide.

Companies Reinventing Themselves In The New Economy

Historically, the world's largest capitalized companies have been a mixed bag of industries. In 1992, the most heavily capitalized companies in their markets were the Industrial Bank of Japan in Japan, United Paper in Finland, Allianz in Germany, British Telecom in the U.K. and Exxon in the U.S. Roll forward to this year, and it is a completely different list. The names are all of companies that have been reinvented or new since 1992, and they're all technology-heavy, "new economy" names. There is NTT in Japan, Nokia in Finland, Deutsche Telecom in Germany, Vodaphone in the U.K. and General Electric in the U.S. This is an enormously significant shift.

Technology-linked new economy companies have taken advantage of an influx of capital, which has propelled their businesses into the largest in the world. This type of shift is not necessarily unprecedented. We've seen throughout history how major innovations have changed both how economies function and how people live.

Deregulation And Digitalization Have Helped Us Move From The Old Economy To The New Economy

Thus, we've made a transition from the physical world to an information world, which is hugely significant when you consider that only 200 years ago, the majority of people in what are now considered the developed nations worked on farms. There was a small manufacturing base and a fledgling services industry. Today, that environment has reversed itself, with service industry employees representing upwards of 80% of the population. Another factor that has contributed to the new, information-driven economy has been the reduction in costs of moving both physical goods and services. Because these cost benefits are more fully reaped if you can move information everywhere, the destruction of many of artificial barriers has also been an enormously significant event driving the new economy over the last decade. While the fall of the Berlin Wall may have seemed to many merely a physical barrier, it was also symbolic of a destruction of trade barriers and massive deregulation, which eventually led to the creation of the euro. Thus, deregulation and digitalization have played a key role in helping us move from the old economy to the new economy.

New Economy Winners and Losers

As part of the new economy, our clients are bombarded by information about the market. One of Lazard's most important functions is helping to clear a path through this information for you. What are our thoughts about Alan Greenspan? What is the Ministry of Finance doing? Are interest rates being lowered? It's important to discuss these issues but it's equally important that, in discussing and explaining these issues, we maintain a global outlook, which will be an even greater factor going forward, as, between digitalization and deregulation, the world is becoming a much smaller planet. The market has understood this transition to the new economy, and as a result, many technology companies have enjoyed a large influx of capital through both venture capital and capital expenditures.

Real technology spending in the 1990s was $2 trillion in the U.S. alone. Forty percent of total Cap-X last year was in technology expenditures. But, in March, we were shown that not all companies were so deserving of this new capital. As the dust cleared, we saw two very different kinds of companies. The first would be the dot.coms, such as eToys and eBay, both of which saw a major drop off in price and productivity. The second would be the enablers, such as the Oracles, the Intels and the companies that are producing products that big companies are using to improve their businesses, which did not see much of a bump during that volatile period.

So, the losers in the new economy are those that don't add value and those that create businesses that nobody really needs, while the winners create products and services that enable companies to maximize their businesses in the new economy.

Old Economy Winners and Losers

Equally important is the fact that there are winners in the old economy too, where another kind of company, an adapter, is present. Adapters are those companies that use enabling technologies to change the way they do their business on a fundamental level. This is not the case with optimizers, which merely work around the edges to make the existing processes a little bit better. The adapters are the companies that will really change the way they do business. General Electric is an example of an adapter because it has improved its business by adopting new technologies, new thinking and by taking advantage of deregulation to change the way it competes.

How To Find Winners In The New Economy

Value versus growth is another issue that will need to be reexamined in the new economy. If you look at where the industries fall, the "value industries" are the ones you'd expect: banks, autos, utilities, while "growth industries" are considered to be pharmaceuticals, computer software, generally industries with a higher price.

To create a successful portfolio in the new economy, the relationship between the price and the productivity of a company needs to be examined. Lazard's philosophy contends that companies that are financially productive and inexpensive compared to their peers are the companies that show true value. Another important factor in determining which companies are going to be successful in the new economy is how they employ technology in their business models. And traditional measures of pricing alone aren't going to help determine that information. Company senior management teams need to be able to explain how they will integrate the latest technology into their business models, and they need to stand by their plans.

When we sit down with management, the important questions Lazard asks are: What are you spending on IT and where are you spending it? Who is driving the process? Do the technology decisions come from top management, or do they fall to the IT department? How broadly is the technology being used, and is it for increased efficiency or as an e-tool? How much creative destruction are you willing to endure? One final, very important question for management needs to be: Have you considered what kind of added value the new economy has given your competitors, or what type of new competitors could stem out of the new economy?

Competition In The New Economy

These are all key questions for traditional and new economy companies. But the consulting business must be examined in this light as well. There are many new competitors trying to capitalize from our existing business, not necessarily all of it, but significant portions of it. The traditional four-step consulting model has become commoditized in recent times. If the new economy has bombarded our clients with information about competing products, what ultimately stops clients from joining rank with competitors? In the end, it is the richness and the strength of the relationship you have with your clients. The critical message for today's financial consultant is to be the trusted advisor that can navigate their client through today's more complex investment environment. ■

About the Author

Bob Morgenthau joined Lazard Asset Management in New York in 1990 as a Vice President and became Managing Director of Private Client Services in 1993. In 1998, he was named Global Head of Marketing and Distribution. Previously, he worked at Shearson/American Express as Vice President of OTC Trading from 1982-84 and then at Shearson Asset Management, Inc. as Senior Vice President and Portfolio Manager from 1984-90. Bob received his BA from Amherst College and may be reached at 212-632-6730.

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